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DOW THEORY LETTERS, INC.

"The Market as Interpreted under the Dow Theory"

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CAPSULE REPORT Industrials continue to act as if they "want" to go up (or at least do not want to go down very far). Rails may (at least temporarily) have "bottomed out". Meanwhile, the mass of stocks on the N.Y.S.E. and the Amex. are marking time or declining. This type of deceptive and frustrating action is frequently seen during the formation of an important top (as was the case during 1959 and 1961).

THE MARKET To a party of men scaling the ice-swept face of Mt. Everest, the constant admonition, "Be careful, boys", would not only be superfluous, it would be downright irritating. I have felt roughly the same way when writing about this market over the past few months.

Since August 30 (see Chart #1), the two Averages (Industrials and Rails) have been caught in a protracted period of divergence. Moreover, the uniformly high volume during this period has only served to emphasize the importance of the divergence. The advance-decline ratio touched its post-crash recovery peak on May 31, following which it turned down. On the second approach to the May 31 peak the A-D ratio gave an important "sell signal" by again turning down, and sinking to successive lows (diverging) in the face of a series of Industrial rallies to new all-time highs. The number of daily new highs have added their "warning message". New highs (Chart #2) have been decreasing with each new thrust of the Industrial Average. From a five-day average of 147 new highs in mid-April, the index has dropped to a recent five-day average of 47 on October 29 (this was the day in which Industrials recorded an historic high of 760.50).

Another simple test may be applied in an effort to gauge the market's "blood pressure". The building of an important trend may be signified by a series of heavily weighted days (these days are often subtly sprinkled over a period of a few months). Any day in which 675 or more issues advance or decline may be termed "a heavily weighted day". This is doubly true if volume is high on such a day.

Since September 1, 1963, the following days produced 675 (or more) advances or declines:

Date	Issues advanced	Volume that day
Oct. 1	688	4.42 (million)
Oct. 3	723	4.51

Date	Issues declined	Volume that day
Sept. 6	679	7.1 (million)
Sept. 9	725	5.02
Sept. 23	751	5.14
Sept. 25	786	6.34
Sept. 26	746	5.1
Oct. 9	697	5.52
Oct. 22	701	6.62
Nov. 6	773	5.6

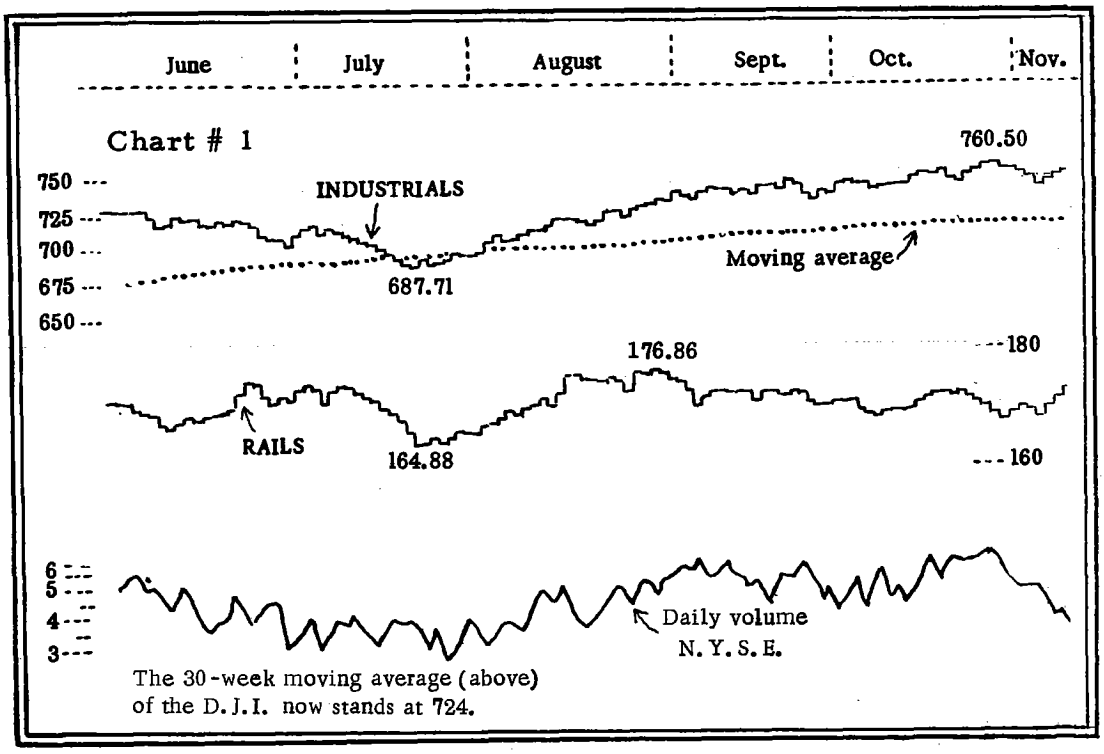
In other words, since September we have had eight heavily weighted "down" days each with accompanying volume of 5 million or more shares. Against this, only two days were heavily weighted on the upside, and volume on those two days amounted to around 4.5 million shares. Conclusion: since September all the "big" days have been downside days. This type of action is generally associated with markets which are in the process of distribution. (It is worth noting that the rally which started on November 7 has, so far, been unable to generate any worthwhile upside volume).

On September 4 (see Chart #2, page 2) the A-D ratio broke decisively below its narrow September- October range. The first important downside level on the A-D ratio is the July low. In view of the renewed weakness in breadth, I feel that there is a good chance that the A-D ratio will shortly penetrate its July low. If this occurs, it will be most important to see whether the Industrial Average will confirm by penetrating its own July low of 687.71.

A downside penetration of the July low by the A-D ratio unconfirmed by Industrials could lead to a good rally (perhaps to a new Industrial high). This is exactly what occurred in late-1959. On the other hand, if the A-D ratio breaks its July low and Industrials confirm, we will have a situation which will appear more like 1962 than 1959.

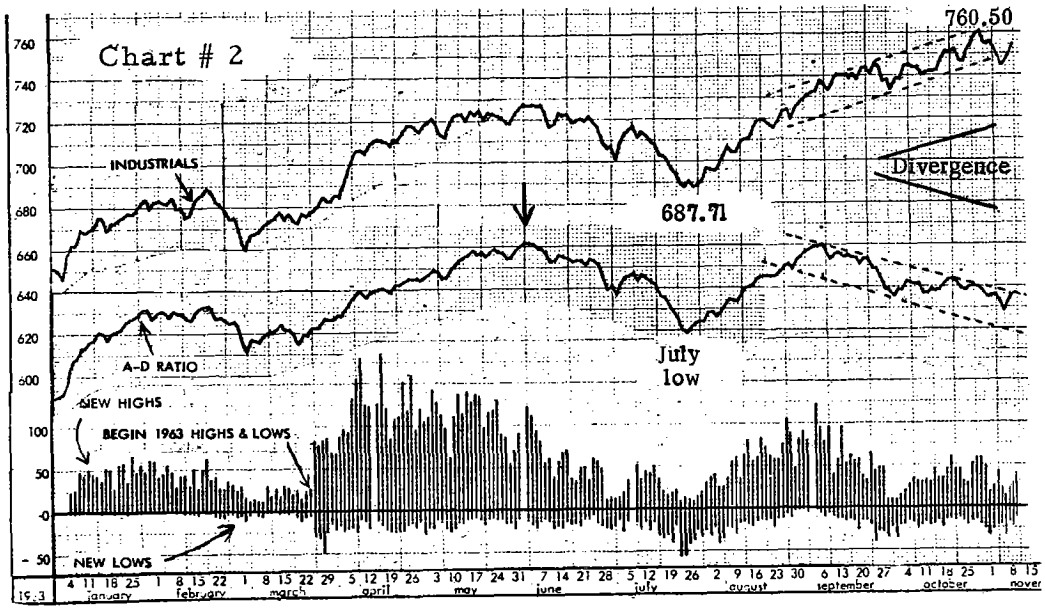
Another consideration: the Rail Average as of November 8 formed an upward zig-zag (Chart #1), and this could imply another assault on the August 30 Rail peak of 176.86. Such a move could also take Industrials to or above their 760.50 high. Thus,

the "whip-sawing" action of the Averages has been part of a long series of "out-of-gear" movements which began in late May, 1963. The total picture is more apparent when we realize the following: In the six months since May 31, Industrials have gained 25 points, Rails have lost about 2 points, Utilities have lost about 2 points -- and the majority of stocks (as measured by the A-D ratio) are considerably lower than they were in May.

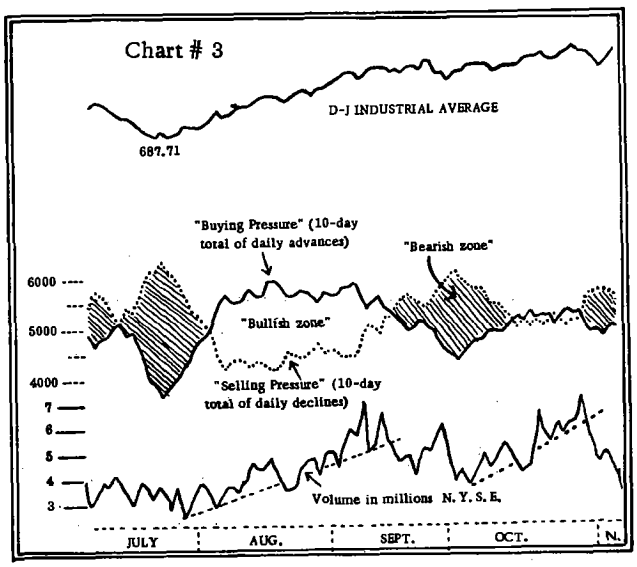


The 30-week moving average (above) of the D. J. I. now stands at 724.

BUYING AND SELLING PRESSURE On October 24, following twelve days of equilibrium (see Chart # 3) the Selling line rose above Buying. This was the second time since mid-September that Selling assumed the dominant position. As seen on the graph, the characteristic of the period since September has been that of persistent selling pressure -- but not of great selling pressure. Neither of the most recent selling areas, in fact, have displayed as much force as was seen in the July selling area. It remains to be seen whether selling will again dissipate itself, or whether the Selling line will climb into the 7000 area and produce something resembling a "sold-out" market condition.

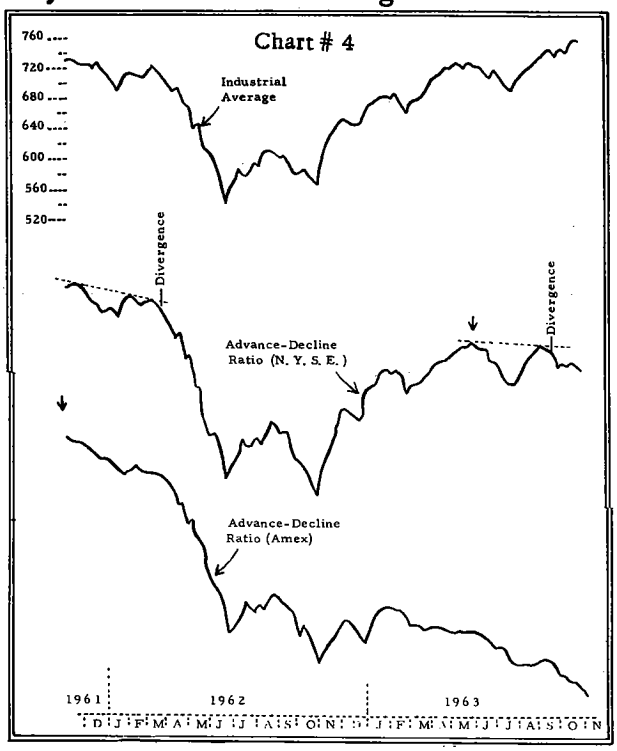


PARTING OF THE WAYS One of the most astounding phenomenons of the past few years is illustrated in Chart #4 (page 3). Here we see the probable reason for the public's persistent skepticism and reticence towards the entire 1962-63 market rise. Note that while the Industrial Average turned up in June, 1962, and continued rising until the present, the trend of the majority of stocks (as measured by the advance-decline ratio) did not reverse to the upside until October, 1962 (four months after the Industrials turned up). Furthermore, the rise in the A-D ratio lasted only seven months -- until October, 1963 (see later section in this Letter). In other words, just about the time the public was getting used to the spectacle of rising prices, the A-D ratio commenced "topping out". And although the public may not have actually been aware of that fact, they doubtlessly "felt it" in that most sensitive of areas -- their pocketbooks.



But even more dramatic than the divergent trend of the majority of stocks on the "Big Board" has been the major (and continuing) bear market on the American Exchange. As seen on Chart #4, the

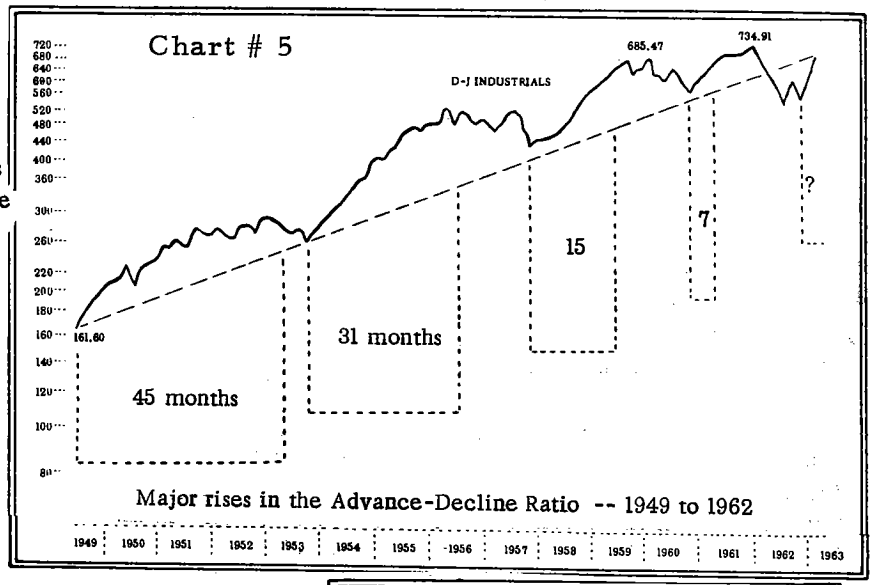
American turned up in October, 1962 (along with the N. Y. S. E.), but by February, 1963, the rise had terminated. Thus, the junior Exchange with its more speculative shares enjoyed only a four-month respite within what must be termed its primary downtrend. Two months ago (in Sept.) the Amex broke below its October, 1962, low on the A-D ratio, and the direction since then has been sharply down for the majority of Amex stocks.



The picture then, is one of an extraordinary concentration of buying in a small number of high-quality issues. Distribution in the majority of issues began in late May (when the A-D ratio on the N. Y. S. E.) turned down, and distribution on the American Exchange never halted -- except for the brief four-month span during late 1962 and early 1963.

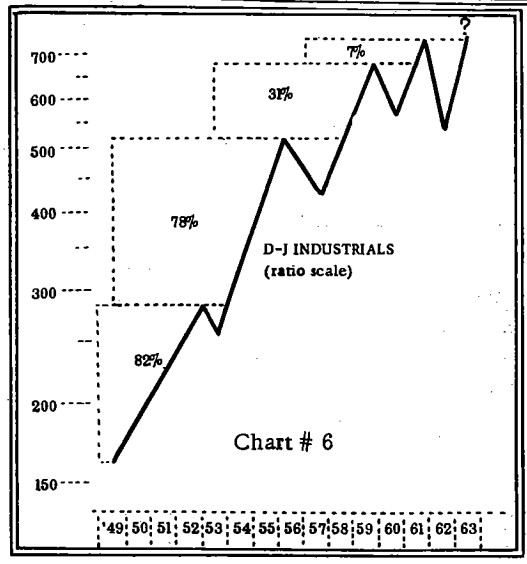
In technical analysis, I have observed that the most persistent force usually wins out -- at least on an intermediate term basis. Therefore, it is now a question of whether the trend of the majority of stocks on both Exchanges will smother the D-J Industrials in their bearish grip, or whether the rallying power of the Industrial Average will stem the pressure toward lower prices in the majority of issues. While anything can happen, past precedent favors the bearish force of the majority.

TIME AND EXTENT Back in Letter 210 (February 20, 1963) I published a chart which traced the major rises of the advance-decline ratio from 1949 to 1963. Judging by the chart (which is again reproduced here), it was evident that each major advance in the A-D ratio since 1949 was of shorter duration than the preceding advance. In Letter 210 I placed a question mark (see Chart #5) next to the rise which began in October, 1962. The implications of the question mark were clear: the 1949-53 advance in the A-D ratio lasted 45 months, the 1954-56 rise lasted 31 months, the 1958-59 advance lasted 15 months, the 1960-61 rise lasted 7 months. Therefore, it was entirely possible that the 1962-? advance would be the shortest of all.



We now know that the A-D ratio (after turning up in October, 1962) reached a peak in May, 1963 -- after a rise of 7 months. To the extent that the study in Letter 210 suggested an extremely short rise in the majority of stocks, the study (in retrospect) proved to be helpful.

In Letter 230 (September 12, 1963) I included another historical study, but instead of dealing with duration, this study concerned itself with the percentage of rise in the Industrial Average on each swing since 1949. Here again (see Chart #6), we note that each successive advance since 1949 tended to add less (in terms of percentages) to the Industrial Average. The last rise (1960-61) took the Industrial Average only 7% beyond its preceding peak, and again I placed a question mark above the most recent movement. The implication of this study was that the advance which began in 1962 would extend by less than 7% beyond the 1961 peak.



To bring this study up to date, if the current rise were to extend a full 7% beyond 1961's Industrial peak of 734.91, the senior Average would advance to 785. At the recent (October 29, 1963) high of 760.50, the Industrial Average had actually extended its gain to about 4% beyond the 1961 high.

But here is the practical point of these studies: the two patterns illustrated in these charts have firmly established themselves over the past 14 years (since 1949). If this market is going to break out of the pattern of shorter rises and decreasing extensions in the Industrial Average, it will certainly constitute an event of the

greatest significance. Such action would necessarily entail (1) the A-D ratio pushing above its May 31, 1963 peak; (2) the Industrial Average pushing strongly above the 785 level. But until one or both of these events occur, my belief is that we should base all our market operation on the hypothesis that the A-D ratio "topped out" in May, 1963, and that the Industrial Average is within a few percentage points of an important top.

STOCKS Of 432 stocks checked here each week, 265 (61%) are now holding above their 200-day moving average, a drop of 3% from the last Letter. The chart below shows the progress of this study and the latest entry. A break below 50% would be an important danger signal. (Tabulations from Quote Digest, 110 N. Lorraine, Wichita, Kansas).

One statistic should make us pause: on November 4, 631 stocks on the N. Y. S. E. were within 1 to 3 points of their 1963 low. This startling figure was compiled by Joe Granville. On top of this, areas of price-breadth divergence are characterized (see Letters 233, 234) by "wild and erratic action." For this reason, I feel that (1) long-term investors should use any market strength as an opportunity to move out of long positions, (2) traders should do a very minimum of trading at this time.

In an inflated and dangerous market such as this one, all transactions should be relegated to the class of speculations. This, of course, is true of short sales in any type of market, since a short by its very nature is a speculation. The quicker a short sale produces a profit the better (there is no tax advantage in holding a short over a period of time, and there is a disadvantage in that dividends must be paid out).

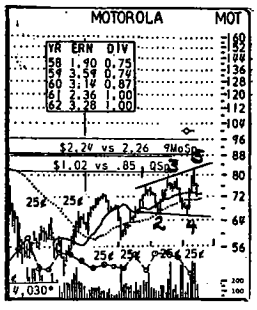
In the last Letter I noted: "Where a stock begins to show a profit, I follow it with stops, thereby limiting potential losses or guaranteeing a profit." Because these Letters (unfortunately) cannot be written and mailed daily, they cannot serve as a "daily trading guide" (a device which would have been extremely handy over the past few weeks).

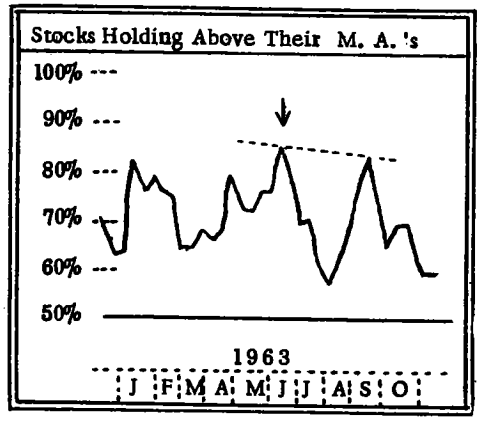
The last Letter with its suggested trading "stops" was mailed prior to the market weakness of November 1-6. On November 6 (short account below) Torrington dropped to 60 1/4, Texaco to 64. A day earlier N. Amer. Av. had touched 46 and Fl. Pow. & Lt. 69 1/2. Those two days produced a maximum profit potential in the short account of 13 points. At the same time Addresso. (long account) wa s stopped out for a 5 pt. loss. Emerson, Goodyear and J & L held essentially unchanged. The writer hopes that the lowered "stop-buy" procedure in the short account produced enough profits to at least offset the loss in Addresso. Proper trading tactics demand that quick paper profits such as the ones which showed up in the short account on November 6 be protected with close stop-buys.

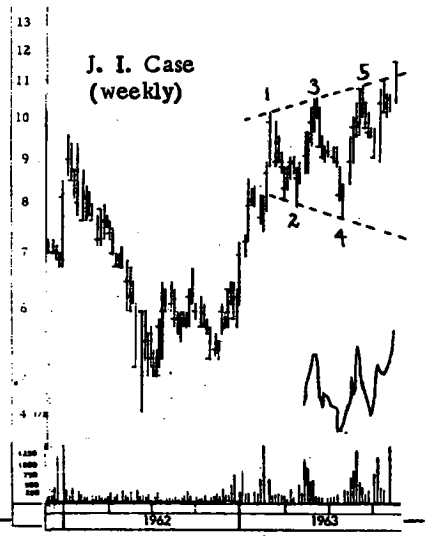
This leaves the account with Emerson, Goodyear and J & L. I have moved the stops up on these stocks in view of what I believe is the steady deteriorating state of the market. I am not adding any new stocks to the portfolio at this time.

One graphic comment: one of the rare "top" formations is the five-point reversal, known as the "broadening formation." These patterns have now appeared in Case and Motorola. Nine out of ten broadening formations are bearish, and it will be interesting to see what happens with these two stocks. Case, in fact has just pushed out of the top of its pattern, and is now as erratic an actor as any stock on the board.

Chart of Motorola courtesy of Quote Digest. Chart of Case courtesy of Traders Research, 1431 Pearl Ave., Alton Illinois 62003.







Date	Name	Price Stock Bought	Price Stock Shorted	Place stops at	Current Price	Current Gain or Loss
Oct. 23	Florida Pow. & Lt.		72	75	73 3/4	Should have been stopped
Oct. 23	North American Av.		48 1/2	50	52	out at a profit
Oct. 23	Torrington Co.		65	65	63	" "
Oct. 23	Texaco		68	73	66 1/2	" "
Oct. 23	Emerson Radio	12 1/4		12	13 1/4	+ 2 1/2
Oct. 23	Addresso-Multi	67		62	64 1/2	- 5 (stopped out)
Oct. 23	Goodyear	42 1/2		39	43	+ 1/2
Oct. 23	Jones & Laughlin	63		59	63	